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In the Supreme Court of the United States.

October Term, 1897.

THE COMMISSIONERS OF THE SINKING Fund of the County of Logan and the County of Logan, Kentucky, appellants,

v.

THE UNITED STATES.

No. 167.

APPEAL FROM THE COURT OF CLAIMS.

APPELLEE'S BRIEF.

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STATEMENT OF THE CASE.

Between October 1, 1862, and July 6, 1872, the county of Logan, Ky., held stock of the Louisville and Nashville Railroad Company, which company paid interest regularly on its bonds, and also from time to time cash dividends on its stock, retaining, however, in each of the years 1865 to 1871, inclusive, an undistributed surplus. (Rec., 7.) The act of June 30, 1864, section 122

(13 Stats., 284), imposed a tax upon all the earnings of railroad companies, as follows:

> Any railroad * * * company indebted for any money for which bonds or other evidence of indebtedness have been issued, payable in one or more years after date, upon which interest is stipulated to be paid, or coupons representing the interest, or any such company that may have declared any dividend in scrip or money due and payable to its stockholders as part of the earnings, profits, income, or gains of such company, and all profits of such company carried to the account of any fund, or used for construction, shall be subject to and pay a duty of five per centum upon the amount of all such interest, or coupons, dividends, or profits, whenever the same shall be payable, and said companies are hereby authorized to deduct and withhold from all payments on account of any interest or coupons and dividends due and payable as aforesaid the duty of five per centum.

The act of July 13, 1866 (14 Stats., 138), amended the section from which the above is taken, but not in any way affecting the present case. Section 44 of the act of June 30, 1864 (13 Stats., 239), also amended by the act of July 13, 1866, and subsequently reenacted as Revised Statutes, section 3220, provided for the repayment of all taxes erroneously or illegally assessed or collected, but the act of June 6, 1872, section 44 (Rev. Stats., sec. 3228), limited the time for presenting applications for repayment to one year in the case of taxes already collected, and two years in the case of those to be thereafter collected. The railroad company paid the taxes required

by these statutes, and made the deductions from interest and cash dividends as authorized thereby, but in so doing it made no exception in the case of interest or dividends payable to public or municipal corporations. The fact that such taxes were paid upon the interest and dividends due the appellants, and that such deductions were made, was not known to the appellants until after the statutory time for applications for a refund of the taxes so deducted. (Rec. 7.)

By a resolution of the directors of November 16, 1867, the railroad company increased its capitalization by 40 per cent, distributing the new shares of stock among the stockholders in proportion to their holdings of the old stock. (Rec. 7–8.)

The act of February 25, 1893 (27 Stat., 447), directed the Secretary of the Treasury and the Commissioner of Internal Revenue to audit and adjust the claims of the appellants and others "for internal-revenue taxes collected on railroad dividends on stock, and on interest on railroad bonds owned" by them in certain companies "to the extent that such taxes were deducted from any dividends or interest due and payable to such boards respectively and which have not been heretofore refunded, * * * any statute of limitations to the contrary notwithstanding." The act also provided that "the amounts, when ascertained as aforesaid and not heretofore refunded, shall be paid out of the permanent annual appropriation provided for similar claims allowed within the present fiscal year."

Under this act the appellants presented a claim to the Commissioner of Internal Revenue for a refund of $17,606.14, which amount was made up as follows:

Tax on cash dividends	$9,645.47
Tax on surplus prior to 1868	6,747.89
Tax on surplus, 1868 and subsequently	1,212.78
Total	17,606.14

It appearing that the county of Logan had sold, May 3, 1879, all its stock in the Louisville and Nashville Railroad Company, the claim for taxes on surplus profits in 1868 and thereafter was subsequently withdrawn. (Rec., 8.)

The Commissioner of Internal Revenue recommended an allowance of $15,397.75, being $9,533.54 on account of taxes on cash dividends and $5,864.21 on account of taxes on surplus, on the theory that this surplus had been converted into the stock dividend of 1867, above referred to. The Secretary of the Treasury approved the allowance and it was formally made. The schedule and the papers in the case were referred to the Fifth Auditor of the Treasury and passed and approved by him. They then went before the Comptroller, and he refused to issue a warrant for the amount or direct the payment of the same, holding that the allowance of the claim for taxes paid on surplus was illegal and unauthorized. He thereupon directed the payment of $9,533.54, and refused to pay any other or further sum. This suit was brought to recover the sum of $5,864.21, which was rejected by the Comptroller. (Rec., 9.)

The court below dismissed the petition, whereupon the claimants appealed. (Rec., 17.)

BRIEF OF ARGUMENT.

Before proceeding to the argument of this case, it is desirable, in order to prevent any misunderstanding, to refer particularly to some of the statements made in the findings of fact and to explain certain apparent inconsistencies between them.

The first finding states that from 1862 to 1872 the Louisville and Nashville Railroad Company "paid cash dividends from time to time, retaining, however, in each of the years 1865 to 1871, inclusive, an undistributed surplus." Also that the company "paid taxes to the United States upon its dividends and upon its surplus earnings, the taxes on the former being deducted from the amount which would otherwise have been paid in full to the stockholders." The word "dividends" in the sentence just quoted above evidently refers to the cash dividends mentioned in the preceding sentence, no other kind of dividends being mentioned in this finding. The sample of a tax return made by the railroad company, as given in the same finding, mentions the amount of dividend declared and the tax thereon, and also the amount of the profits over the dividend declared and the tax upon the same. It is clear that this return relates exclusively to the tax on a cash dividend and the tax on surplus profits over and above that cash dividend.

The second finding relates to an increase of stock of 40 per cent made by resolution of the directors of the railroad company and distributed among the stockholders. The resolution of the directors, which is given in full, provides for "an increase of the stock of 40 per cent," and does not refer to the payment of any tax upon such

increase of stock or any deduction from such increase of stock on account of any tax. Furthermore, the resolution does not state that this "increase of stock of 40 per cent" is a distribution to the stockholders of the surplus profits previously undistributed, nor does it state that the amount of the new stock has anything to do with the amount of undistributed profits. The only reference whatever in the resolution to the earnings of the company concerns future increases of stock, and as to them only to the extent of providing that such increases shall be made whenever the net annual earnings of the company shall be sufficient to pay interest accruing upon the indebtedness of the company, provide a sinking fund sufficient to pay the bonded debt of the company as it falls due, and to pay 6 per cent on the stock. The amount of increase of the stock would, therefore, seem to have been determined with reference to the capacity of the net annual earnings to pay a dividend on that stock, rather than with reference to the amount of surplus profits in hand.

The same finding states the par value of the capital stock in 1867 as $5,638,600, and the par value of the stock dividend thereon as $2,131,500. As 40 per cent of $5,638,600 is $2,255,440, there would seem to be a patent error in the court's statement as to the par value of the stock dividend in 1867 to the extent of $123,940, unless in point of fact a portion of the stock was held by the corporation itself, as is often the case, so that the distribution of the stock dividend to the stockholders did not require the issue of new stock to the full extent of 40 per cent upon the total capitalization. Certainly the difference between

$2,255,440 and $2,131,500 can not be accounted for by any payment of tax, because, first, it does not appear that any tax was paid which decreased the rate of the stock dividend below 40 per cent, and, further, the difference in the amount, $123,940, is considerably more than 5 per cent (the tax rate in 1867) upon $2,255,440.

The third finding states that the county of Logan made a claim in 1893 for a refund of the tax on cash dividends and on surplus. This shows clearly that the claim was not one for refund of any tax paid on a stock dividend.

The fourth finding states that the Commissioner of Internal Revenue "recommended the allowance of said sum." The words "said sum" can not refer to the total amount of the claim presented by Logan County, as given in the third finding, because that finding states that a portion of that claim was withdrawn. In using the words "said sum" the court below has evidently overlooked the fact that it had not previously stated what precise amount was found by the Commissioner on audit and adjustment of the claim of Logan County; but this amount is shown by the Commissioner's letter of September 28 to the Secretary of the Treasury, a copy of which is annexed to the petition in this case (Record, pp. 3 and 4), to have been $9,533.54 on account of taxes on dividends, and $5,864.21 on account of taxes on surplus, making an aggregate of $15,397.75, which is evidently the amount referred to in Finding IV as "that sum." Finding IV also states that the Comptroller held that "the allowance of the claim for taxes paid on

account of stock dividends was illegal and unauthorized." The allowance referred to obviously means the allowance which the Commissioner stated that he made on account of "taxes on surplus," it appearing that the theory on which the latter allowance was made was that the surplus was converted into a stock dividend, but not that any tax had ever been paid on the stock dividend as such.

The fifth finding purports to recite what had taken place in 1890-91 in regard to a claim of the city of Louisville, which was paid by the act of June 30, 1891 (26 Stats., p. 867). The propriety and finality of that payment comes before this court in case No. 105, but it is submitted that the greater part, if not all, of this finding is absolutely irrelevant in the present case. The first part of the finding, including the Commissioner's letter of January 24, 1891 (Rec., 9-10), is plainly irrelevant, because it does not appear that these statements and this letter were ever communicated to Congress at all, at least in the shape in which they appear here; while the relevancy of the latter portion (viz, the communications actually submitted to Congress, Rec., 10-11) is at best very doubtful, as it does not appear that Congress had those communications in mind when the act of February 25, 1893 (under which the present case arises), was passed, or that its action in passing that act was in any way influenced by the statements made to it in 1891. This finding may therefore be disregarded.

Certain statements which appear in this finding should, it is submitted, be disregarded on another ground, namely, that they are conclusions of law and not statements of

fact. The finding says that cash dividends were declared upon this stock; that "there was also a large amount of undistributed surplus belonging to the city upon which stock or scrip dividends were issued," and "these cash dividends and the undistributed surplus which was converted into stock or scrip dividends were held by the officers of the Government to be subject to taxation, and taxes were assessed and collected according to the terms of the statute in force at the time of the respective collections." The words "there was also a large amount of undistributed surplus belonging to the city" involve not only a conclusion of law as to the ownership of that surplus, but a conclusion which is absolutely at variance with the law as laid down by the court below in this case. The opinion states (Rec., 16):

> The controlling fact in the case is that the undistributed profits of the company were *not* the property of the claimant when the tax on them was paid.

If that was true in law of the county of Logan, it was equally true of the city of Louisville, and hence it is clear that this statement must have appeared in the finding through inadvertence on the part of the court below. The statement in the finding that the undistributed surplus belonged to the city, as also the reference to the surplus as having been converted into stock dividends, are, moreover, inconsistent with the findings of fact made by the court below in the case of the city of Louisville (case No. 105), which merely stated that there was a surplus and that there were stock dividends in 1867 and

1880, but did not state that there was any necessary connection of any kind between the two.

In explanation of the peculiarities of Finding V, it is submitted that a reference to the record in the court below, if such reference can properly be made by this court, will show that the first part of this finding was a part of the statements of fact which the appellants' counsel requested the court to make. The court having found, with sufficient precision, the facts in regard to the claim of Logan County, and having decided against that claim, evidently thought that a finding as to facts relating exclusively to the claim of the city of Louisville was not of very special importance, and while it was willing to make a finding in regard to those facts, it did not consider the precise language used as carefully as it would otherwise have done.

It appears, therefore, from these findings as a whole, that the taxes with which the court is concerned in this case were those upon cash dividends and upon surplus profits only; that no taxes were paid upon the stock dividends which figure in this case, and that no deduction was made therefrom on account of the payment of any tax, but that the Commissioner of Internal Revenue in making his allowance acted on the theory that the payment of taxes on surplus profits was equivalent to a payment of taxes on a subsequent stock dividend and a diminution of that dividend to that extent.

The questions as to whether a tax on surplus profits under the act of June 30, 1864, should be regarded as a tax on a stock dividend, and as to whether the act of

February 25, 1893, authorized the allowance of any claim on account of taxes paid upon undistributed surplus having been fully considered in pages 32 to 52 of the brief in the case of the *United States* v. *The Commissioners of the Sinking Fund of the City of Louisville*, No. 105, that argument need not be repeated here. It is only necessary to consider certain contentions made by the appellants' counsel in his brief in the present case.

THE CONTENTION THAT THE SURPLUS WAS DISTRIBUTED.

Appellants' counsel states (brief, p. 13) that "this surplus fund was *expressly* distributed in the form of a stock dividend." There is absolutely nothing in the record from one end to the other to warrant this statement. The only *evidence* as to the stock dividend is the resolution of the directors of the railroad company of November 16, 1867 (Rec., 8), and this resolution does not refer at all to the surplus profits previously earned. It declares that in the future the stock shall be increased by 10 per cent whenever the net annual earnings shall make it possible to pay a dividend of 6 per cent upon the whole amount of stock, including such increase. This declaration of the future policy of the company is important as showing how the directors regarded a stock dividend. They intended to apply increased net annual earnings to the payment of dividends upon an increased capitalization, a policy that would effectually prevent any substantial additions to the property represented by the capitalization. In other words, the stock was to be

"watered" whenever the earnings admitted of a dividend on the "water" as well as on the stock previously existing. The amount of "water" was to be measured by the earning capacity of the company, not by the amount of its surplus, and hence that surplus was in no sense to be distributed by the addition of the "water" to the stock. Undoubtedly a stock dividend provides a means of distributing *future* earnings, but only in the form of cash dividends on an increased capitalization. It can not distribute past or present earnings, and it does not appear that the directors of the railroad company ever supposed that it could.

In support of his statement that "this surplus fund was *expressly* distributed in the form of a stock dividend," appellants' counsel cites, first, the statements of Commissioner Mason and Acting Secretary Nettleton, as also those of Acting Commissioner Wilson and Acting Secretary Hamlin (see appellants' brief, p. 20), statements which are merely evidence of the opinions held by those gentlemen, but are in no sense evidence of the facts. Secondly, counsel cites a part of the fifth finding (appellants' brief, 13, 14, 20), containing the words "undistributed surplus belonging to the city upon which stock or scrip dividends were issued," "undistributed surplus which was converted into stock or scrip dividends." It has already been stated that these parts of the finding are not statements of fact, but conclusions of law, and hence must be disregarded, whether inadvertently made, as they manifestly were, or not.

Apparently the sample portion of a tax return (appellants' brief, p. 15), is also referred to in support of the

same statement that "this surplus fund was *expressly* distributed in the form of a stock dividend," but in point of fact it makes against that statement. This is manifestly not a complete return, being without caption, date, or signature. It is merely an extract relating to two matters, the cash dividend and the "profits *over* dividend," and to the tax of 5 per cent which was levied upon each. The words "5 per cent of dividend retained as excise tax" refer to the sum of $11,637.62 (the tax on a cash dividend) only, and have no reference to the sum given on the second line ($74,265.78), which represents the tax on the surplus profits, and is put in the same column as the tax on the dividend merely for the purpose of addition, in order to reach a total. Appellants' counsel assumes that the words "5 per cent of dividend retained as excise tax" apply to the whole column and to every sum that appears therein, and indicate that the tax upon "profits *over* dividend declared" was "retained" from some "dividend" paid to the stockholders. It should not take much penetration to see that a sum of money can not be at one and the same time a dividend and "profits *over* dividend," or that the last line of this extract has nothing to do with taxes on dividends, and that the only dividends to which the extract relates are cash dividends, from which alone, as far as this extract is concerned, a tax was retained, and to which alone, as far as this extract shows, the act of February 25, 1893, related. Hence where counsel says "the whole dividend was ours and we received only 95 per cent of it" (appellants' brief, p. 16), this can, in truth, refer to a cash dividend only.

THE CONTENTION AS TO THE PRACTICE OF THE RAILROAD COMPANY.

Appellants' counsel states that—

> The practice was, as has been frequently set forth, for the railroad, whenever it proposed to declare a stock dividend, to set apart a certain amount out of their net earnings, which amount included the 5 per cent tax. After deducting the tax from the amount set apart, the balance was distributed into [in?] a stock dividend. The stockholder, and not the railroad, suffered the diminution. * * * The stock dividend by its express term covered the surplus that had accumulated. (Appellants' brief, 16–17.)

If the word "cash" were substituted for the word "stock" in the above passage, the statement (except the last sentence) would be true; but as it stands it both flatly contradicts the record and describes an impossibility. Not merely is there no evidence that "a certain amount out of their net earnings" was ever set apart for distribution as a stock dividend, or that any tax was ever deducted from the amount so set apart, but the resolution of November 16, 1867, (Rec., 8) shows clearly that such was not the practice. The resolution contains not one word about setting apart a dollar of the net earnings, but it shows that the practice was to increase the capitalization whenever it appeared that the net earnings sufficed to pay a 6 per cent cash dividend on the capitalization as increased, and there was no deduction from such increase of capitalization, or stock dividend, on account of any tax. No such deduction was in fact

possible, because no tax was paid on the stock dividend, and the taxes on surplus were paid during a period of three years or more before the stock dividend was declared. After a tax has once been paid it can not be "set apart" and deducted.

THE CONTENTION AS TO SECTION 121 OF THE ACT OF 1864.

Appellants' counsel states that the act of 1864 required all stock dividends to be taxed, and provided (by section 121) that when a stock dividend included any part of the surplus or contingent fund, the tax previously paid on such surplus should be deducted (appellants' brief, p. 17); but even conceding that stock dividends come within the letter of the act of 1864, it does not follow that every stock dividend has been returned for taxation and the proper tax paid thereon, and hence in any claim for a refund such return and payment must be proved. In the present case there is no such proof, and the findings indicate that no such return or payment were ever made. The railroad company evidently considered that as the stock dividend neither added to nor took away anything from its property or its stockholders' property, it was unnecessary even to enter it on the tax return.

The effect of the proviso in section 121 of the act of 1864 is considered in the brief for the United States in case No. 105 (pp. 48–51), and it is only necessary to add that even if this proviso applied to stock dividends it would not have obviated the need of returning those dividends for taxation, with a statement of the precise amount of tax to be deducted, and it would not now

obviate the need of proof of such return and deduction. The need of these can not be obviated by suggesting that a tax on surplus and a tax on a stock dividend "are in the eye of the law one and the same." (Appellants' brief, p. 18.) Unless the collector had the opportunity of seeing whether the tax paid on the surplus equaled in amount the tax due on the stock dividend, he would be unable to know whether they were "in the eye of the law one and the same" or not.

THE CONTENTION AS TO THE HISTORY OF THE ACTS OF 1890 AND 1893.

Appellants' counsel contends (brief, pp. 21–24) that the history of the passage of the acts of 1890 and 1893 shows that Congress intended to authorize a refund of taxes paid on surplus. He says: "While the first bill in 1890 was pending, and before its passage, both the House and Senate were expressly informed of the exact nature of the transaction," and in support of this statement he refers first to a report made to the Senate in 1890, upon the petition of the city of Louisville, for a refund of the taxes paid on its dividends. This report is *not in the record*, and the mere fact that it is contained in a public document (Sen. Rept. No. 640, 51st Cong., 1st sess.) can not make its contents the subject of judicial notice. This court will take notice of the official publication of such a document, so as to dispense with proof of the genuineness of the papers it contains, but it will not take judicial notice of them unless they are such as are entitled to judicial notice wherever they are found. There is just one part of the report which can be judicially noticed, viz,

the findings and judgment of the circuit court for the district of Kentucky in *Commissioners of Warren County* v. *Speed*, and these, through some inadvertence, appellants' counsel has so misquoted as to totally alter the meaning.

The findings as printed.	*As quoted in appellants' brief.*
(3) That the county of Warren, at the time of the several payments, owned stock in the said railroad company subscribed thereto by said county and paid for * * * and also other stock issued to said county by said railroad company for dividends which were paid by and in the stock so issued to said county, and the above amounts were paid as the taxes claimed to be due to the said United States on the dividends declared by said company on the stock of said county in the said railroad company.	In the judgment of the court, the taxes in controversy were spoken of as "upon other stock issued to said county by said railroad company for dividends which were paid by and in the stock so issued to said county."

The finding merely states that Warren County had acquired stock of the railroad company in two ways, viz, by original subscription and by stock dividends, and that certain sums were paid as taxes on dividends declared on such stock, both the original and that afterwards acquired by stock dividend. The finding does not state that any of these taxes had been paid on stock dividends, but counsel quotes it as stating that the taxes were "upon other stock issued * * * for dividends which were

paid by and in the stock so issued," i. e., upon stock dividends.

The finding in the Warren County case therefore merely shows that Congress was informed, in a rather round about and inferential way, that the railroad company had declared stock dividends, but not that they had been taxed, or that taxes had been deducted from them. The rest of the report, even if it could be judicially noticed, would show no reference to stock dividends whatever.

In support of his contention as to the intention of Congress in the act of 1893, appellants' counsel cites certain reports not in the record and containing, apparently, nothing which can be judicially noticed. Even if they could be judicially noticed, however, they would be worth very little. The court has repeatedly held that the debates in Congress are not appropriate sources of information from which to discover the meaning of the language of a statute passed by that body, and for the reason that "it is impossible to determine with certainty what construction was put upon an act by the members of a legislative body that passed it by resorting to the speeches of the individual members thereof." (*United States* v. *Freight Assn.*, 166 U. S., 290, 318, and cases there cited.) It can make no difference in this respect whether the opinions of individual members are expressed in speeches or in reports. Conceding that Congress may have been informed that certain counties wished to make claim for a refund of taxes on stock dividends, and that those counties were named in the act of 1893, it does not follow that Congress undertook to decide in favor of claims

of that character. All that it did, as the court below has held, was to remove the bar of the statute of limitations of claims to recover taxes, but it left it to the officers of the Treasury and to the courts to decide whether the claims themselves were entitled to be allowed.

THE CONTENTION AS TO THE UNCONSTITUTIONALITY OF THE INCOME TAX.

The final contention of appellants' counsel is that the tax imposed by section 122 of the act of June 30, 1864, was unconstitutional under the ruling in *Pollock* v. *Farmers' Loan and Trust Co.* (158 U. S., 601), so that no money acquired by the United States under that act can lawfully be retained by it, except where claims are barred by some statute of limitation. Even if this contention were sound, it could not affect the present case, because the tax was not paid by the appellants, either directly or indirectly, but was assessed against the property of the railroad company and paid by it, and should therefore be refunded to it alone, if a refund were required.

It is therefore submitted that the judgment of the court below should be affirmed.

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